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Supreme Court, U. S.

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No. 95-928

CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

JOHN W. ATHERTON, JR., ET AL.,

Petitioners,

vs.

FEDERAL DEPOSIT INSURANCE CORPORATION, in its
capacity as receiver for CITY SAVINGS, F.S.B.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

PETITIONERS' REPLY BRIEF

DOUGLAS M. KRAUS
Counsel of Record
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM
919 Third Avenue
New York, New York 10022
(212) 735-3000

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ARGUMENT

In its brief in opposition ("Opp. Br.") to the petition for a writ of certiorari in this case, Respondent Federal Deposit Insurance Corporation (the "FDIC") concedes that the fundamental premise of the Third Circuit majority's ruling below -- that 12 U.S.C. § 1821(k) ("Section 1821(k)") does not apply to federally-chartered depository institutions and that "federal common law" therefore supplies the source of law in this case -- is erroneous. (Opp. Br. at 12) Yet the FDIC attempts, nevertheless, to justify the result reached by the court below, arguing in effect that it reached the right result for the wrong reasons. It does so by relying on arguments that have been rejected by each of the other courts of appeals that have considered this issue, and which even the Third Circuit majority declined to adopt. These arguments fly in the face of the plain language of Section 1821(k), and lead to a conclusion that simply cannot be reconciled with this Court's holdings in *O'Melveny & Myers v. FDIC*, ___ U.S. ___, 114 S.Ct. 2048 (1994), *City of Milwaukee v. Illinois*, 451 U.S. 304 (1981), and *United States v. Texas*, ___ U.S. ___, 113 S.Ct. 1631 (1993). Review by this Court is warranted to correct this manifest error. (See Point I, *infra*)

In reality, the FDIC's concession that the majority below erred in concluding that Section 1821(k) had no application to federally chartered institutions supplies yet another compelling reason why a writ of certiorari should be granted in this case. Taken together with Respondent's further concessions that the opinion below creates a clear conflict among the Circuits, and its acknowledgment that this case presents an issue of law that is of vital importance to the resolution of not only this case, but also the scores of other related pending FDIC and RTC cases, as well as future cases that may be brought by the FDIC, it is now clear that the parties agree that this case presents virtually every factor customarily recognized as warranting review by this Court. (See Point II, *infra*)

Finally, the FDIC argues that certiorari should be denied because the admittedly important legal issue raised in this case should not be addressed on an interlocutory appeal. This is a remarkable position for one who argued in the court

below that interlocutory review was essential in this case. The very purpose of 28 U.S.C. § 1292(b) is to permit appellate review where a case presents a controlling question of law as to which there is substantial ground for difference of opinion, and an immediate appeal may materially advance the ultimate termination of the litigation. Here, the district court, the court of appeals and the parties themselves have all agreed that this is the case. This Court has often granted certiorari in such cases -- particularly where, as here, a clear split among the Circuits exists on the issue presented for review. Moreover, considerations of judicial economy and fairness to the litigants weigh especially strongly in favor of review in this case, since (1) petitioners are individuals who are financing this complex litigation out of their own pockets, and (2) sending this case back to the district court for resolution of the standard of care issue will at best precipitate yet another round of interlocutory appeals and at worst could result in a lengthy trial using an erroneous legal standard -- in short, a huge waste of time and money for the parties and the courts. (See Point III, *infra*)

I

RESPONDENT CONCEDES THAT THE OPINION BELOW IS BASED ON AN ERRONEOUS PREMISE, AND ITS EFFORTS TO JUSTIFY THE RESULT REACHED BY THE PANEL MAJORITY ARE WHOLLY UNAVAILING

The fundamental flaw in the opinion below is its astonishing assertion that Section 1821(k) -- a *federal* statute, made applicable by its terms to all *federally*-insured depository institutions -- has no applicability to federally-chartered institutions such as City Federal. However, the FDIC now concedes that Section 1821(k) applies to federally-chartered institutions such as City Federal, and that the Third Circuit majority's holding to the contrary is erroneous. (Opp. Br. at 12)

Specifically, the FDIC acknowledges:

Section 1821(k) provides that the FDIC may bring an action against an officer or director of an

"insured depository institution." 12 U.S.C. 1821(k). "Insured depository institution" is defined in FIR-REA as "any bank or savings association the deposits of which are insured by the [FDIC] pursuant to this chapter." 12 U.S.C. 1813(c)(2). The FDIC insures both federal and state chartered institutions.

(Opp. Br. at 12, n.8) Thus, Respondent states, Section 1821(k) "should be read to apply to federally chartered institutions." (Opp. Br. at 12)

Nevertheless, the FDIC argues that the result reached by the majority is sound, even though its underlying premise was not. Its arguments in favor of the result below, however, exhibit the same flaws as the majority's opinion.

First and foremost, the FDIC, like the majority below, puts the proverbial cart before the horse in interpreting Section 1821(k). It reads Section 1821(k)'s legislative history as revealing a single legislative intent -- to preempt so-called state "insulating" statutes -- and then twists the plain language of the statute to make it conform to this purpose.¹ This Court has repeatedly instructed that the first step in statutory analysis is to examine the actual statutory language used by Congress. *Kaiser Aluminum & Chem. Corp. v. Bonjorno*, 494 U.S. 827, 835 (1990). Here, the actual language of Section 1821(k) makes clear that gross negligence is the legal standard selected by Congress to apply in cases such as this.

The FDIC asserts that because Section 1821(k) states that officers and directors "may" -- as contrasted with "may only" -- be held liable for acts of gross negligence the statute is simply a non-exclusive grant of rights. This argument was properly rejected by the Fifth, Sixth and Seventh Circuits for two reasons; not only would such a reading undermine the very cause of action that the statute creates, making it little

¹ In fact, Section 1821(k)'s legislative history makes clear that preempting state insulating statutes was not the only thing Congress had in mind when it enacted the statute. Congress also sought to avoid setting the liability threshold so low as to discourage the best qualified individuals from serving as officers and directors of savings institutions.

more than a piece of advisory legislation, but it also places undue emphasis on the word "may," a word that cannot reasonably be read to modify the substance of the provision. *FDIC v. Bates*, 42 F.3d 369, 371 (6th Cir. 1994); *Resolution Trust Corp. v. Miramon*, 22 F.3d 1357, 1361-62 (5th Cir. 1994); *Resolution Trust Corp. v. Gallagher*, 10 F.3d 416, 420 (7th Cir. 1993). Significantly, even the majority below declined to base its decision on this ground. *Resolution Trust Corp. v. CityFed Financial Corp.*, 57 F.3d 1231, 1237, n.7. (3d Cir. 1995).

The FDIC also tries to limit the effect of the substantive portion of Section 1821(k) by reading the savings clause to preserve actions under federal common law, which it asserts would be governed by a simple negligence standard. This construction violates the well-established rule of statutory construction that a savings clause cannot be allowed to supersede a specific substantive provision. See e.g., *Morales v. Trans World Airlines, Inc.*, 504 U.S. 374, 384-85 (1992); *International Paper Co. v. Ouellette*, 479 U.S. 481, 494 (1987). If the savings clause were construed to preserve federal common law actions for simple negligence, then the language of the substantive sentence of Section 1821(k), which specifically enunciates a cause of action for gross negligence, would be rendered meaningless surplusage and a nullity. *Bates*, 42 F.3d at 372; *Miramon*, 22 F.3d at 1361-62; *Gallagher*, 10 F.3d at 420.

Respondent also maintains that there is no conflict between the decision below and this Court's decision in *O'Melveny & Myers v. FDIC*, ___ U.S. ___, 114 S.Ct. 2048 (1994). However, what the FDIC contends here is precisely what it contended, unsuccessfully, in *O'Melveny* -- that a provision of FIRREA "should be read as a nonexclusive grant of rights to the FDIC receiver, which can be supplemented or modified by federal common law." *Id.* at 2054. This Court rejected this argument in *O'Melveny*, and should do so again in this case. Indeed, the FDIC's nonexclusive-grant-of-rights argument is especially absurd since in *O'Melveny* this Court specifically listed Section 1821(k) as one of the provisions of FIRREA

that created a specific federal rule of decision, and thus supplanted federal common law. *Id.*

The FDIC attempts to turn *O'Melveny* on its head by asserting that federal common law does not supplement FIRREA, but rather that FIRREA supplements federal common law. Therefore, Respondent argues, the two are completely compatible.

This argument completely ignores this Court's explicit pronouncements in *City of Milwaukee v. Illinois*, 451 U.S. 304, 313-14 (1981), and *United States v. Texas*, ___ U.S. ___, 113 S.Ct. 1631, 1634 (1993), that federal common law is "subject to the paramount authority of Congress," and that "when Congress addresses a question previously governed by a decision rested on federal common law the need for such an unusual exercise of lawmaking by federal courts disappears." In contrast to the rule respecting presumption of state laws, it is not necessary for Congress to "affirmatively proscribe" the federal common law rule in order to abrogate its application. *City of Milwaukee*, 451 U.S. at 315; *United States v. Texas*, 113 S.Ct. at 1634.

Here, as the FDIC concedes, Congress spoke directly to the standard of liability applicable to officers and directors of federally-chartered, federally-insured depository institutions in RTC and FDIC actions. In such a case, FIRREA does not supplement federal common law; FIRREA supplants federal common law. Indeed, this is the conclusion reached by every court of appeals that has addressed this issue. See *Resolution Trust Corp. v. Frates*, 52 F.3d 295, 297 (10th Cir. 1995) (citing *City of Milwaukee*); *Bates*, 42 F.3d at 373 (citing *United States v. Texas*); *Miramon*, 22 F.3d at 1360 (citing *City of Milwaukee* and *United States v. Texas*); *Gallagher*, 10 F.3d at 424-25 (same). The same result is warranted here.

Because the opinion below was premised upon the admittedly erroneous conclusion that Section 1821(k) has no applicability to federally-chartered depository institutions, and because the resulting ruling is incompatible with both the plain language of Section 1821(k) as well as this Court's prior holdings respecting the use and application of "federal

common law," this Court should issue a writ of certiorari to review and reverse the decision below.

II

THERE IS NO DISPUTE THAT THIS CASE PRESENTS VIRTUALLY EVERY FACTOR RECOGNIZED TO WARRANT A GRANT OF CERTIORARI

It is now clear that Respondent agrees that this case presents virtually every factor that this Court has indicated would support the granting of a writ of certiorari.

First Respondent concedes that there is a clear conflict in the Circuits.² This Court has often stated that a square and irreconcilable conflict among the Circuits on the same issue of federal law is an extremely weighty factor in deciding to grant certiorari. *See, e.g., Vimar Seguros Y Reaseguros, S. A. v. M/V Sky Reefer*, ___ U.S. ___ 115 S. Ct. 2322 (1995); *McElroy v. United States*, 455 U.S. 642, 643 (1981); *Marks v. United States*, 430 U.S. 188, 189 (1977).

Moreover, the FDIC acknowledges the signal importance of this issue, both to the resolution of this case and to the resolution of literally scores of other pending cases brought by the FDIC and its predecessor, the RTC, against officers and directors of federally-chartered thrift institutions. Indeed, the RTC argued, at the district court level and again to the court of appeals, that this issue presents a controlling question

² Citing *FDIC v. McSweeney*, 976 F.2d 532 (9th Cir. 1992), *cert. denied*, 113 S.Ct. 2440 (1993), and *FDIC v. Canfield*, 967 F.2d 443 (10th Cir.), *cert. dismissed*, 506 U.S. 993 (1992), Respondent argues that the split is not as one-sided as Petitioners believe. (Opp. Br. at 14) However, neither *McSweeney* nor *Canfield* is relevant to this case. Both cases involved displacement of state law, not federal common law. *See McSweeney*, 976 F.2d at 537; *Canfield*, 967 F.2d at 444. Moreover, assuming that *McSweeney* and *Canfield* did, in some way, support Respondent's assertion that Section 1821(k) does not preempt federal common law, the consequence would be to make the existing split in the Circuits even more pronounced than it currently is, and the need for this Court to resolve this conflict would be even more, not less, pressing than it is at present.

of law as to which there is substantial ground for difference of opinion and that an interlocutory appeal from the district court's order would materially advance the ultimate termination of the litigation. Both the district court and the court of appeals agreed with this argument, and certified this issue for interlocutory appeal. (Pet. App. A-67, A-68)

Finally, the FDIC admits that the reasoning of majority below was unsound. As discussed in Point I, *supra*, Respondent now concedes that Section 1821(k) applies to federally-chartered institutions such as City Federal, and that the Third Circuit's holding that Section 1821(k) has no application whatsoever to such institutions is erroneous. (Opp. Br. at 12) This Court has noted that certiorari is appropriate where the court below has decided an important question erroneously. *See, e.g., New York Transit Authority v. Beazer*, 440 U.S. 568, 571 (1979); *Perma Life Mufflers v. International Parts Corp.*, 392 U.S. 134, 136 (1968); *Williams v. Lee*, 358 U.S. 217, 218 (1959).

It is thus undisputed that this case presents virtually every significant factor generally recognized to warrant the grant of a writ of certiorari. Accordingly, the writ should issue here.

III

THE COURT SHOULD HEAR THIS CASE EVEN THOUGH IT IS AN INTERLOCUTORY APPEAL

Respondent urges the Court to deny certiorari because the Third Circuit's decision arose in the context of an interlocutory appeal brought pursuant to 28 U.S.C. § 1292(b). (Opp. Br. at 8, n.6) This assertion is paradoxical, to say the least, since in the court below Respondent urged that an interlocutory appeal was appropriate and, indeed, essential here; it is, moreover, entirely without merit.

Even before Congress passed 28 U.S.C. § 1292(b), this Court often granted certiorari in cases that came up on interlocutory appeal where, as here, there was an important issue of law that was fundamental to the further conduct of the case and that would otherwise qualify as a basis for certiorari. *See,*

e.g., *United States v. General Motors Corp.*, 323 U.S. 373, 377 (1945); *Land v. Dollar*, 330 U.S. 731, 734 n.2 (1947). See also Robert Stern, Eugene Gressman, Stephen Shapiro and Kenneth Geller, *Supreme Court Practice and Procedure*, § 4.18 (1993).

By passing the Interlocutory Appeals Act, Congress indicated that it favored interlocutory appeals where, as here, the district court and the court of appeals agreed that there is "a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order [appealed from] may materially advance the ultimate termination of the litigation." 28 U.S.C. § 1292(b). Since the Act's passage, this Court has often granted certiorari in cases appealed pursuant to 28 U.S.C. § 1292(b). See, e.g., *Vimar Seguros Y Reaseguros, S. A. v. M/V Sky Reefer*, ___ U.S. ___ 115 S. Ct. 2322 (1995); *United States v. 92 Buena Vista Ave.*, 507 U.S. 111 (1992); *Kansas v. Utilicorp United, Inc.*, 497 U.S. 199 (1990).

Like the court of appeals decisions in *Vimar Seguros*, *92 Buena Vista Ave.*, and *Utilicorp United*, the decision below has created a conflict among the Circuits. The decision below also conflicts with recent decisions of this Court, contradicts the plain language of Section 1821(k) and violates well-established rules of statutory construction. Further, this case is of widespread importance both in numerous pending and future cases, and to the banking and thrift industries as a whole. In addition, the district court, the court of appeals and every one of the parties in this case has asserted that the question now presented for certiorari is "a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order [below] may materially advance the ultimate termination of the litigation." 28 U.S.C. § 1292(b).

Significantly, three of the other four courts of appeals to address this issue addressed it on interlocutory appeal, either pursuant to 28 U.S.C. § 1292(b) or Fed. R. Civ. P. 54(b). See *Frates*, 52 F.3d at 296; *Miramón*, 22 F.3d at 1358; *Gallagher*, 10 F.3d at 418. In each of these cases, the district court found

and the court of appeals confirmed that the requirements of 28 U.S.C. § 1292(b) had been met or that there was "no just reason for delay" under Fed. R. Civ. P. 54(b). That four courts of appeals have made this same determination demonstrates that this issue is truly a critical question affecting the entire body of cases that are outstanding in this area and is appropriate for resolution now.

Moreover, to deny certiorari at this time and send the parties back to the trial court for a determination of the appropriate standard of care under federal common law would result in an enormous waste of judicial resources. The district court's decision almost certainly will result in a second interlocutory appeal to the court of appeals and a second petition for a writ of certiorari. If certiorari is not granted at that time, the parties and the district court will then proceed to try this extremely complex case,³ using a possibly erroneous legal standard, following which, the losing party will again appeal to the court of appeals, and then again petition for certiorari, in order to determine the standard of care that it believes should have been applied at trial.

In addition, should certiorari be denied, courts and litigants in scores of similar cases in the Third Circuit and elsewhere will spend substantial resources struggling to define the standard of care for officer and director liability under federal common law,⁴ when it is not even clear that federal common law applies. Finally, this situation cries out for prompt resolution by this Court, since Petitioners, like hundreds of other defendants in these cases, are private individuals financing their defenses out of their own pockets, and are facing an

³ This litigation involves hundreds of thousands of documents, and involves three complex acquisition, development and construction loans. The trial of this case will take weeks, and possibly even months.

⁴ It is noteworthy that the only guidance that either the court below or the FDIC has given as to the content of a federal common law of officer and director liability is two cases that were decided several decades before *Erie R. Co. v. Tompkins*, 304 U.S. 64 (1938).

adversary (the United States government) with virtually limitless resources.

CONCLUSION

For the foregoing reasons, and the reasons set forth in the Petition for a Writ of Certiorari, this Court should grant a writ of certiorari to review the Third Circuit's decision that Section 1821(k) does not supplant "federal common law" regarding the standard of liability for officers and directors of failed federally chartered financial institutions, and should summarily reverse that decision.

Respectfully Submitted,

DOUGLAS M. KRAUS
Counsel of Record
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM,
919 Third Avenue
New York, NY 10022
(212) 735-3000

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